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ACTION PLAN
for the
CITY OF SCOTTS VALLEY

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Prepared by
Housing Authority of the County of Santa Cruz
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Introduction

This Action Plan has been prepared by the Housing Authority of the County of Santa Cruz for the City of Scotts Valley. The purpose of the strategy, as initially conceived and described in the City's request, was to identify those actions the City could take in order to implement all the policies and programs relating to affordable housing as set forth in its Housing Element and design a set of programs consistent with the Set Aside Housing Fund requirements.

As the City's Housing Element already describes the housing needs of various income groups, this report does not duplicate that element by re-assessing demand for affordable housing. Rather, it accepts the needs identified by the City and suggests approaches to developing housing to meet those needs.

This action plan outlines several actions Scotts Valley can take to facilitate the development of affordable housing. The Housing Element already provides a framework for a number of these.

Key Observations

This section provides a concise overview of the market, institutional and regulatory context in which affordable housing efforts will take place.

- The most obvious market consideration in the development of new affordable housing is the price of land in the City. A component of price is the supply of appropriately zoned, suitably sized developable parcels.
- The City's Housing Element indicates that land constitutes 35% of total development cost for housing in Scotts Valley.
- The Housing Element estimates that there are 1,022 acres of vacant, residentially designated land within the City which, at the time of the Element's preparation, could accommodate 2,180 dwelling units. In addition, there are a number of single family lots which could accommodate small in-law units. Commercially zoned land may accommodate mixed use projects.
- Many jurisdictions use redevelopment funds to create affordable housing opportunities. Scotts Valley has one redevelopment project area, which is expected to generate a total of \$440,219 in housing set aside funds for 1991 and 1992. California State redevelopment law requires that 20% of a redevelopment agency's tax increment be set aside and placed into a low-moderate income housing fund.
- The Housing Authority of the County of Santa Cruz operates the Section 8 rental assistance program throughout much of the County, including Scotts Valley. This program provides rental

subsidies to property owners on behalf of eligible very low-income tenants. Roughly 40 Scotts Valley households participate in the program.

- Article 34 of the State Constitution requires that a local government obtain voter approval before developing, constructing or acquiring low-rent housing. Scotts Valley currently does not have Article 34 Authority.
- The City has a housing element which currently has not been certified by the State Department of Housing and Community Development (HCD) to be in compliance with State law.
- The City does not currently operate a homeowner rehabilitation program.

Housing Needs

The Housing Element has identified the following areas of housing need.

- Based upon a 7.7% average annual employment growth between 1981 and 1990 Scotts Valley will have a projected job base of 6,627 in 1996. In 1990 Scotts Valley had a total of 3,449 housing units. In order to meet the increase in the employment sector Scotts Valley would have to provide a total of 4,664 units. This represents an increase of 35% in the housing stock.
- Calculations developed by the Association of Monterey Bay Area Governments (AMBAG) for use by local communities in preparing their housing elements indicate that a total of 1,507 dwelling units should be built in Scotts Valley during the 1988-96 period in order for the City to meet its share of the region's housing needs. This total is further distributed by income category as follows:

| | | | |
|-----------------------|-----|-------|-------|
| Very low-income | 426 | units | 20.4% |
| Low-income | 236 | units | 15.2% |
| Moderate income | 281 | units | 20.4% |
| Above moderate income | 564 | units | 44% |

- A second useful indicator of need for affordable housing is the number of low-income households who overpay for housing (i.e., pay more than 25% of their gross income for housing). For Scotts Valley the data is as follows:

| | |
|---|-------|
| Total number of low income households | 1,079 |
| Households overpaying for housing | 351 |
| Percent of low income households overpaying | 32.5% |

- Overcrowding affects 3% of the households, a total of 104 households.
- A total of 1,378 or 16% of the households are 65 years of age or older.
- Single parent households represent 6% of the households, and female headed households represent 4.6% of the households.
- Of the total housing units in Scotts Valley 74.4% are owner occupied and 25.6% are renter occupied.
- There are five mobile home parks with 749 units.
- Land costs represent 35% of the cost of development in Scotts Valley.

Action Plan

In order to create a successful housing program, the City will have to integrate local housing needs and quality of life concerns with the economics of feasible project development and the regulations of available funding sources. A brief discussion of these "ingredients" may prove helpful in thinking about the most appropriate approach for Scotts Valley.

Housing Needs

The Housing Element established a goal to develop affordable housing to meet the needs created by the expansion in the employment sector. Additionally, the Housing Element sets a goal to develop 97 very low, low and moderate income units per year. This means a total of 485 units in the next five years. In order to meet that goal the City needs to create an aggressive program that maximizes the resources and opportunities available to Scotts Valley.

Quality of Life

Quality of life is an important concern for many California communities today. As cities reach build out and infrastructure reaches capacity or a level of service unacceptable to residents, several local governments have responded by enacting various controls.

The aggressive development of affordable housing should not compromise the existing quality of life for Scotts Valley residents. Through careful design and choice of developers the City can pursue the creation of affordable housing without compromise to the residents.

Economic Feasibility

The economic feasibility of a housing development depends on an array of factors, the most important of which are:

- the price of land,
- construction costs and development fees, and
- cost and terms of financing.

The City's actions affect these factors in different ways. The City influences the price of land through its regulatory powers, may add to construction costs by imposing certain development standards, controls development fees through the charges it establishes to offset project impacts and recoup planning and building processing costs, and, unless it is selling tax-exempt revenue bonds or otherwise providing financial assistance, does not affect the cost of financing.

If the City is to create a successful affordable housing effort, it must find ways to address those costs over which it has some control.

An appropriate methodology for evaluating proposed projects and identifying project costs, particularly those over which the City has control, is to consider proposed projects in terms of "gaps". The "gap" is the shortfall attributable to the project financing which makes the project unable to proceed.

Additionally projects are viewed in terms of feasibility and affordability gaps. The feasibility gap is the shortfall when the project is viewed as a 100% market rate project and still cannot be built given current market conditions. For example, a developer basis the feasibility of a project on the assumption that the rents received will generate enough funds to support the loan payment. If this not possible the project than is said to have a "feasibility gap". The affordability gap is the gap which is created if a project is feasible as a 100% market rate project, but becomes to costly when affordable units are included in project evaluation.

In order to better understand the "gap" it is necessary to determine the affordability of housing costs on a monthly basis. These costs are then used to determine the financing capabilities of a project. The following is a brief explanation of how these costs are calculated:

Affordable Housing Cost Calculations

| |
|--------------------------------|
| Income as Percentage of Median |
| X 30% |
| Affordable Housing Cost |
| <u>Less Utility Allowance</u> |
| Affordable Rent |

Homeownership

| | |
|---------------------------------|--|
| Income as Percentage of Median | |
| X 30% | |
| Affordable Housing Cost | |
| Less Property Taxes | |
| Less Insurance | |
| Less Private Mortgage Insurance | |
| Less Homeowners Dues | |
| <u>Less Utility Allowance</u> | |
| Affordable Mortgage Payment | |

For further discussion of feasibility and affordability gaps please see Appendix "A". Appendix "A" describes a 15 unit apartment project with both an affordability and a feasibility gap. Also set forth in the appendix are specific project assumptions and identification of gaps based on current market conditions in Scotts Valley.

Financing Program Regulations

Individual federal and State programs for affordable housing development are discussed in more detail in the Resources section. Presented below is a summary of requirements common to the key financing programs.

The majority of programs provide financial assistance for the development of rental as opposed to ownership housing. This is in response to data which shows that renters tend to be poorer than homeowners and, therefore, have a greater need for affordable housing. Few of today's low-moderate income housing finance programs require that all the units in a development be affordable. Instead, programs focus on a mix of income groups so as to better reflect the community in general. Rents for these households are restricted to 30% of income, adjusted for unit size (e.g., a family of three is presumed to live in a two bedroom apartment. The affordable rent is \$561 less a utility allowance of \$35). These requirements must be in effect for between 15 and 30 years.

A second approach allows 40% of a project's units to be rented to low-income households (i.e., those earning no more than 60% of the median income; (Specific median income information is presented in Appendix "B", this format is provided for ease of inserting new information on an annual basis)

Income limits for owner-occupant programs are usually higher because such programs assume the target population for homeownership is the low-moderate income group (80%-120% of the median income) rather than the very low-income households.

Generally, income limits range from 90%-110% of the median income, again adjusted for family size.

What price can households with such incomes afford? Assuming 30% of income is paid for housing, a mortgage interest rate of 9.5%, a 30-year loan term, and a 10% downpayment, home prices corresponding to the income range in the preceding paragraph are \$99,105-\$131,281. Some programs, such as the Mortgage Credit Certificate Program administered by the Housing Authority with which Scotts Valley is participating, have house price limits set by federal statute. In Scotts Valley this limit is \$235,440 for a new home and \$205,470 for an existing home. Income limits and affordable rents/mortgage payments for the categories of households to be assisted are shown in Appendix "B".

Housing expense for rental includes a utility allowance. Under homeownership, housing costs include principal, interest, mortgage insurance, hazard insurance, homeowner dues and taxes. The discussion contained in this section illustrates the complexity of developing affordable housing and the number of objectives, regulations and needs that must be considered and addressed in order to create a viable housing effort. These are not unique to Scotts Valley; most California communities face these issues and many have developed successful housing programs that meet their local needs. Key to their success are:

- The judicious use of staff and financial and non-financial resources and powers;
- An ability to involve the neighborhood in which a development will be located;
- The commitment to making a project "work"; and
- The willingness to prioritize project processing and consider modifications to development standards if appropriate.

City Roles

Before discussing a proposed set of programs for Scotts Valley, it may be useful to think about the various roles the City should and should not play in creating and operating an affordable housing effort.

The most appropriate roles for the City are that of facilitator and, in certain cases, lender. As facilitator, the City could:

- Locate suitable sites for the development of affordable rental and for-sale housing;
- Use local regulatory powers and incentives to create housing opportunities;

- Sell tax-exempt housing revenue bonds to provide financing for the construction of multi-family developments;
- Advise for-profit and non-profit developers of financing programs for affordable housing;
- Inform interested developers of City programs and policies relating to affordable housing;
- Support financing applications submitted by developers for affordable projects that meet the City's goals;
- Clarify types of loans and financing mechanisms such as affordability gap, predevelopment, site acquisition and second mortgage programs that provide a standard vehicle for City participation in rental, homeownership, and mobile home programs; and
- Priority processing for projects with affordable housing through the City's planning and building review process.

The role of lender can be more complicated than that of facilitator, as the City will be required to evaluate any request for financial assistance and determine how much is actually needed and the terms under which it will be provided. The provision of any City funding should be guided by the following financial considerations:

- Maximize leveraging of City funds by requiring investment in the project by the developer, private lenders, and/or State and federal agencies;
- Use limited local dollars only to fill the "affordability gap," i.e. the amount of financing not supportable by project income due to the lower affordable rents/prices, not the feasibility gap;
- Loan, rather than grant, City funds;
- Use local resources as the catalyst for investment of private and other public moneys; and
- Provide financial assistance to those projects that are economically sound and where the developer has the experience to carry out the type and scale of project proposed.

Terms of repayment of City funds would be clearly spelled out in a loan agreement, and the affordability requirements (e.g. the number of low-moderate income units, the prices/rents for the low-moderate income units, the term for which the units must remain affordable, etc.) would be contained in a regulatory agreement.

Scotts Valley may not wish to assume the roles of project developer or manager. Private developers, non-profit organizations and the Housing Authority are equipped to handle actual development, and the City may find partnership more effective than competition with these entities.

Recommended Housing Program

Any housing program developed by the City must be sustainable in the long run. To achieve this, efforts must be based on a clear understanding of the political, fiscal and physical limits which can constrain development.

The City's initial project(s) should be fairly modest in scale, gradually increasing in size and complexity. The strategy is to achieve a series of successes and then build on these over time. When faced with competing requests for resources, the City should selectively choose those that 1) address its identified objectives, and 2) contribute to its strategy for success.

There are several actions which Scotts Valley can take to begin to put together a viable housing program. Generally, these can be grouped into site identification and control; financial resource development; regulatory incentives and powers; and capacity building.

Site Identification and Control

The City's Housing Element lists an array of programs for new housing development, several of which represent local land use actions designed to "create" sites for new housing. Some programs call for an inventory of available sites or an evaluation of the reuse potential of land in the City, while others create sites through density bonuses and air rights. Scotts Valley is to be commended for recognizing the need to have a sufficient supply of land for housing, for without suitable sites available, an affordable housing program will never succeed.

The Housing Authority is currently identifying potential sites for acquisition and development.

Financial Resource Development

Second in importance to having a site is the ability to assist in the financing of a project. Typically a city's contribution would be used for "hard costs" (e.g. to write down the cost of required infrastructure) or, in the case of a non-profit developer, certain predevelopment costs (e.g. architecture and engineering); it is not used to provide working capital, fees or profit to the builder. Normal lending procedures would be followed in evaluating loan requests (appraisals, title reports, toxic studies, project

proformas, sources and uses budgets, etc.) and all loans would be secured by a deed of trust on the property.

There are two resources potentially available to Scotts Valley that could be used to further the City's housing efforts:

- Community Development Block Grant (CDBG) and HOME; and
- 20% redevelopment set-aside.

Scotts Valley's Housing Element recognized the merit of targeting these resources for affordable housing development by recommending the use of the following two programs:

Community Development Block Grant/ HOME

Community Development Block Grant (CDBG) and HOME funds can be used for an array of activities to support development of affordable housing including site acquisition, certain planning studies and predevelopment costs, and off-site improvements. Where CDBG cannot be used for the construction of the dwelling units, HOME can be used for construction.

If the City identifies specific programs then it should plan to apply through the State for both programs.

Redevelopment Set-Aside

State redevelopment law requires that 20% of the tax increment collected by a redevelopment agency be set aside into a Low-Moderate Income Housing Fund. Monies in the Fund can be used to acquire sites, pay for predevelopment costs, install both on- and off-site improvements, construct the dwelling units and subsidize rents. Funds can also be used to rehabilitate existing housing occupied by low-moderate income owners or tenants.

The 20% set-aside funds are required to be used inside the redevelopment project area unless the legislative body makes a finding that such housing located outside the project area will be of benefit to the redevelopment project. The finding can usually be made if the housing to be constructed outside the project area is in close proximity to the project area or the implementation of the project has generated demand for low and moderate income housing.

A key requirement under section 33334.4 of CRA is that the locality must target its resources to the identified income group needs.

This requirement simply means that the total production of units with Set Aside funds must be in the following categories:

| | |
|-----------------|-------|
| Very low income | 20.4% |
| Low Income | 15.2% |
| Moderate Income | 20.4% |

As a threshold the Agency should establish this as an initial requirement for projects financed with set aside funds.

Federal and State Resources

There are a variety of governmental housing finance programs which would be available to develop lower income units in Scotts Valley. These are described in Appendix I: Resources, and, with the exception of the following, will not be repeated here.

Regulatory Incentives and Powers

Some cities have studied the impact on their housing needs caused by commercial and industrial development. In an attempt to mitigate impacts identified with job/housing imbalance, some cities have created linkage programs which require payment of a fee for affordable housing based on an established standard.

Capacity Building

To create a successful housing program, it is anticipated that the following tasks and duties will be required by the City of Scotts Valley:

- Undertake the preparation of a vacant, surplus and underused land inventory;
- Administer the compliance monitoring for all housing units created through density bonus, tax-exempt bond programs and set-aside funds;
- Operate a housing rehabilitation loan program;
- Serve as the clearinghouse for information and regulations on affordable housing programs;
- Locate and obtain control of suitable sites (with assistance from appropriate real property and legal staff);
- Prepare requests for proposals for development of affordable housing, evaluate project proposals and recommend projects, and negotiate loan terms for affordable projects;
- Design and implement a first time buyer program.

Program Objectives

Key to Scotts Valley's success in developing affordable housing is to create a program that meets the City's needs and fits in with the scale of the City. Careful attention must be paid to devising objectives that match the City's resources and are possible within the current constraints.

Of course, other resources will be required in addition to the City's funds. The objective is to end up with a debt service payment that can be covered with the amount of income derived from the project, given the fact that below market rents are being paid. The financing of affordable housing today is quite complex and often calls for a custom blend of resources to get the rent or sales prices down to an amount that a low-moderate income household can afford (see the Affordable Payments listed on page 8). For example, a 20-unit elderly project in the City of Healdsburg in Sonoma County included 7 different funding sources, or one funding source for every 3 units. Although this example may be a bit unusual, it is not at all uncommon to see today's rental projects financed with a combination of:

- Rental Housing Construction Program funds from State HCD;
- An allocation of federal and State Low Income Housing Tax Credits;
- Local funds (usually to cover land costs); and
- A conventional loan from a bank or savings and loan which is perhaps using a subsidy from the Federal Home Loan Bank's Affordable Housing Program.

In keeping with the City's Housing Element, possible objectives for the next five years could include the nine programs described below.

1. Financing the development of affordable family housing in potential development sites and provide site acquisition funds.
2. Develop a gap loan program to assist in developing affordable housing structured to accomodate elderly, single family or disabled.
3. Work with experienced private sector developers to create first time buyer opportunities for median income households by providing down payment assistance to first time buyers.
4. Start up and operate a Citywide housing rehabilitation loan program. If this program is funded primarily by CDBG, City

funds would be required for staff and certain pre-rehabilitation costs only (e.g., appraisals, title reports, etc.). Possible use of other State funds.

5. Provide predevelopment assistance to affordable housing developers (establish criteria for eligible pre-development loans for public purpose and projects).
6. Require mitigation for affordable housing requirements created by residential development in the Redevelopment Area. Mitigation should be limited to the provision of affordable units within the development.
7. Work with local employers to create an effective employee housing assistance program.
8. Augment the MCC program with the use of silent seconds or down payment assistance for first time homebuyers each year.
9. Encourage projects that provide on-site childcare.

Success in achieving the aforementioned objectives is more likely if the projects meet as many of the following criteria as possible (it is unlikely that any one project will meet all of these):

- Meet an identified, high priority need.
- Be of relatively modest size (no larger than 50 units) unless done in conjunction with a sophisticated developer experienced in affordable housing development and management.
- Be a mixed income development with units set aside for low and very low-income families (unless the project is less than 10 units, in which case all units can be affordable).
- Have the appropriate general plan designation and/or zoning.
- Not require extraordinary site preparation or development costs, including toxics removal.
- Have the support of the neighborhood in which it will be located.
- Meet the affordability requirements of the most likely federal and/or State funding programs.
- Have the support of local housing advocates and community leaders.
- Be appropriately designed to be compatible with (not necessarily identical to) the scale and character of the surrounding area.

- Not rely on an overall relaxation of development standards for feasibility.

Conclusion

As in any plan or strategy, the key to its success is the commitment to the objectives and the commitment of resources. The City's Housing Element established aggressive goals for affordable housing. This Action plan lays out eight programs that are currently being used by cities throughout California to implement the Housing Element goals and redevelopment set-aside requirements. Critical to the success of the Action Plan is the support and inclusion of the community in adopting the Plan.

Next Steps

1. Staff should review and submit comments for changes to the Action Plan by the Housing Authority.
2. A final Action Plan should be submitted to the Housing Task Force with a presentation by the Housing Authority.
3. Submit the plan to the Redevelopment Agency Commission and City Council for adoption.
4. Prepare an implementation schedule and plan.

APPENDICES

Appendix I: RESOURCES

There are a number of financial and other resources available to Scotts Valley to implement its housing initiatives. These include federal and State programs as well as locally raised money, redevelopment set-asides, and surplus government or institution-owned property.

This section discusses some of the major resources, which are then summarized along with others in the chart that follows. It is important to recognize that today's high development costs require a combination of sources to make a project feasible; gone are the days when a developer could receive all its financing from a single source.

A. Surplus Property

Local governments, other public agencies, schools and churches may own land they no longer need and which Scotts Valley can purchase for affordable housing. If a government - owned surplus site is not suitable for residential development it can be sold and the proceeds dedicated for a lower income housing project on another site.

School districts and local governments are required by State law to notify the local housing authority of the availability of surplus property before selling such property on the open market. Rarely are there any bargain sales; properties are sold for full assessed value or leased on a long-term basis. Most agencies/institutions of surplus property need the revenue from a property sale for their other operations and cannot afford to sell for a below market price. Given the difficulty in finding suitable sites, the City's primary objective with respect to surplus land should be to secure the property and only secondarily to obtain a reduced price.

B. Redevelopment Set-Asides

State law requires, with some exceptions for temporary deferral, that redevelopment agencies set aside 20% of their tax increment into a Low and Moderate Income Housing Fund to be used to increase, preserve or improve their supply of low and moderate income housing.

To the extent tax increment monies are used to finance new rental development or substantial rehabilitation, the project must meet certain affordability restrictions for the longest feasible time, but in no case less than 15 years. When funds are used for homeowners, affordability restrictions are for at least 10 years. Affordability requirements would be structured as deed restrictions which survive transfer of title or other changes in use.

Failure to expend excess tax increment set-aside monies within specific time frames could result in their mandatory transfer.

C. In-Lieu Housing Funds

Many California cities have inclusionary zoning ordinances which require developers of projects of more than 5 units (sometimes 10) to sell/rent a portion (usually 10 - 20%) of the units to low-moderate income households. Instead of actually providing the affordable units on site, these ordinances usually allow a developer to pay an "in-lieu" fee to the city. This resource is especially valuable for its flexibility, i.e., a local government can decide how the funds will be used.

D. Community Development Block Grant (CDBG)

CDBG monies are fairly flexible and can be used for pre-development costs (site options, soils investigations, architect and engineer costs, etc.) which can be difficult to finance from other sources due to timing constraints.

E. Tax-Exempt Bonds

Cities, counties, housing authorities and redevelopment agencies all can issue tax-exempt bonds to finance the construction or acquisition and rehabilitation of rental housing, or to assist first-time homebuyers with mortgages for the purchase of new or existing housing. Such financing enables the developer to borrow funds at rates which are typically 2-3% below conventional rates. Bonds are paid off with revenues from the housing.

1. Multifamily Requirements:

- a. In order to sell multifamily revenue bonds, an issuer must request and receive a private activity bond allocation from the California Debt Limit Allocation Committee (CDLAC) prior to issuance. Such allocations are very competitive. CDLAC allocation meetings take place in February, April, June and August with applications due the tenth of the month preceding the meeting.
- b. The entire property must be maintained as rental for as long as bonds are outstanding, but in no case for less than 15 years after half of the units are initially occupied.
- c. At least 20% of the units must be affordable to and occupied by households at or below 50% of median income adjusted for household size for at least 15 years after

half of the units are occupied. State law requires that all affordable units be leased at rents based on 30% of 50% of median income.

- d. The affordable units described above must be of comparable size and quality to all other units in the development and must be dispersed throughout the development.
- e. Bonds can be used both for new rental construction and for acquisition and rehabilitation of existing rental properties where the cost of rehabilitation equals at least 15% of the amount of bond proceeds.

Certain of the above requirements are less restrictive in the case of a bond issue done solely to finance a project for a non-profit developer. More importantly however, a non-profit issue does not need a CDLAC allocation.

- 2. Single-Family Requirements (currently expired; requires Congressional re-authorization in this year's budget bill):
 - a. An issuer must request and receive a private activity bond allocation from the California Debt Limit Allocation Committee (CDLAC) prior to issuance or (more likely) cooperate with CHFA bond issues.
 - b. The income of the borrower may not exceed 90 - 115% of median depending upon household size and whether homes are new or existing housing.
 - c. The maximum sales price is established by the IRS, based upon 90% of the average area purchase price, and in Contra Costa County is currently \$181,170 for a new home and \$148,410 for an existing home.
 - d. The borrower must be a first-time homebuyer (a person who has not had an ownership interest in a home for the past three years).

F. Mortgage Credit Certificates (MCC)

MCC's provide first-time homebuyers with incomes of \$38,830 (1-2 persons) or \$40,595 (3 or more persons) with an annual tax credit of up to 20% of the annual interest paid on their mortgages (the remaining 80% is deducted as usual). To be effective in increasing borrower eligibility and affordability, the City can require participating lenders to take the credit into consideration in underwriting the borrower's mortgage. Some localities use either bonds or credits in conjunction with a locally designed second mortgage program. Like tax-exempt bonds, an agency or local government desiring to use MCC's must apply for and receive an allocation from CDLAC or use CHFA's MCC program.

Based on the program guidelines, the following is an example of the MCC program's impact on affordability:

| | <u>With MCC</u> | <u>Without MCC</u> |
|---|-----------------|--------------------|
| Purchase Price | \$135,900 | \$135,900 |
| Closing Costs | 4,077 | 4,077 |
| 20% Down Payment | 27,180 | 27,180 |
| Loan Amount | 112,970 | 112,970 |
| Monthly Payment: (30 year loan @ 10%) | 990 | 990 |
| Less 20% MCC credit on mortgage payment: | | |
| Effective payment with 20% credit on mortgage payment | 990 | 792 |
| Taxes and Insurance | 155 | 155 |
| Total Housing Cost | <u>\$1,145</u> | <u>\$947</u> |

In light of the overall average City sales price of \$250,000 an MCC program would probably be workable in only a few neighborhoods, and primarily among condominium units.

G. Low-Income Housing Tax Credits

As part of the 1986 Tax Reform Act, a new tax credit was made available to developers of new or rehabilitated rental housing. Use of the credit is possible if at least 20% of the completed units are rented to households at or below 50% of median income (or 40% of the units are rented to households at or below 60% of median). Rents may not exceed 30% of the maximum income limits based on household size (less applicable utility allowance). Affordability must be maintained for an initial 15-year compliance period and a second 15 year extended period, subject to certain State actions.

The tax credit amount is based upon the total development costs or rehabilitation costs of the very low-income units. The credit to the developer is either 9% (if 100% privately-financed) or 4% (for projects receiving certain federal assistance including tax-exempt bonds) of the development cost of the low-income units. The credit is received each year for a period of 10 years from the time the project is placed in service. For example, if a developer constructs a 100-unit project at the cost of \$60,000 per unit and 20 units are set aside as low-cost, the owner is eligible for an annual tax credit of \$108,000 (9% of \$60,000 x 20) per year for ten years (provided no other defined federal subsidy is used).

The credit is allocated to eligible developers by the Tax Credit Allocation Committee (TCAC) upon receipt of an application which has been reviewed and approved by either the city or county in which the project is located. The process is extremely competitive as TCAC receives many more applications than can be funded.

H. Affordable Housing Program (AHP)

The Federal Home Loan Bank recently announced it is accepting applications for its newly-created Affordable Housing Program, established pursuant to FIRREA. Approximately \$20.172 million is available in the eleventh district, 60% of which was allocated in the first round. Applications for the second round were held August 31, 1990; awards will be announced in November 1990.

The AHP will use dedicated Bank earnings to subsidize by 1-5 points the interest rate of financing provided by member institutions for affordable rental or ownership projects. Subsidies will be provided through below-market advances at fixed rates for 10 year terms, directly with 30 year terms, or through other creative mechanisms. The amount of the subsidy is limited to that necessary to bring an eligible household's housing payment down to 28% of its income.

I. California Housing Finance Agency (CHFA)

The California Housing Finance Agency administers a number of rental and ownership housing programs funded with the proceeds of tax-exempt bonds sold by the Agency. Essentially, the single-family programs provide low-moderate income first-time homebuyers with below market interest rate mortgages and/or second mortgages to assist with the downpayment; the rental programs provide financing for the construction of apartment units, including second mortgages from CHFA's Housing Trust Fund.

J. California Department of Housing and Community Development

In 1988 California voters passed two major initiatives: Proposition 77, the California Earthquake Safety and Rehabilitation Program, and Proposition 84, the Housing and Homeless Bond Act. The initiatives resulted in two significant resources that are available for affordable housing development in California. Both programs are funded through General Obligation Bonds and are administered by the California Department of Housing and Community Development (HCD).

1. California Housing Rehabilitation Program (CHRP)-Proposition 77

This program has both owner occupant and rental components. For rental projects, two types of activities are eligible:

- a. The rehabilitation of unreinforced masonry multifamily buildings where 70% of the units are occupied by low-income households; and
- b. The acquisition and rehabilitation of substandard low-income rental housing.

For rehabilitation alone, the loan term is for not less than twenty (20) years; for acquisition and rehabilitation, the term is for thirty (30) years. Loans are at 3% simple interest. Rents for the assisted units are limited to the State's affordable rent requirements. Funds are available from HCD on a continuous basis.

2. Rental Housing Construction Program (RHCP) - Proposition 84

Under this program, the State makes available a 3% simple interest loan for construction and/or take out financing for development and construction costs. In turn, the developer is required to provide 30% or more (depending on the amount of the loan) of the units for occupancy by low and very low-income households for forty (40) years. Initial rents may not exceed 30% of 35% of area median as adjusted for family size and less the utility allowance. After the first year, rents are adjusted according to the State's rent increase formula.

K. Local Opportunities

1. Planning Documents

California State law requires that each local government develop a housing element as part of its general plan and revise that element not less than every five years. The housing element must contain an analysis of housing needs for various groups, an inventory of sites suitable for residential development, objectives and programs to address the identified needs, an evaluation of past housing efforts, and an analysis of constraints on the rehabilitation and development of housing.

Preparation of certain specific plans or area plans represents another opportunity to encourage the development of lower income housing. Mechanisms could include the designation of sites suitable for mixed income housing projects or an inclusionary program tailored to the plan area. At the very least, large tracts of land being up-zoned should provide for some affordable housing.

2. Annexations

As cities build out to their current boundaries, annexations within the LAFCo sphere of influence will be proposed. Local governments should view such annexations as opportunities to create affordable housing either within the annexation area or through the use elsewhere of in-lieu fees paid by the annexing developer.

3. Density Bonus Requirements

State law requires that a city or county grant a 25% density bonus to a developer in exchange for an agreement that 1) 20% of the units be affordable to lower income households, or 2) 10% be affordable for very low-income households, for a period of 30 years.

4. Local Trust Funds

Some local governments have created trust funds for low-moderate income housing. A trust fund is a pool of monies dedicated to housing whose source is fairly stable. San Mateo County, for example, capitalized its trust fund with the sale proceeds from a County-owned surplus site, and San Francisco is studying a possible increase in its real estate transfer tax.

Appendix 2: SPECIFIC PROGRAMS

In general, there are a number of ways in which communities have assisted homeownership and rental housing. The following four program models illustrate the most effective ways in which a city such as Scots Valley can finance affordable housing projects. These models represent lending mechanisms that, once they are established, can be applied to the full range of project types: shelters, transitional housing, mobile home parks, rental housing, family, elderly, disabled, mixed income and first time buyers. The program outlined below are the vehicles necessary for a community to finance housing.

Due to the small size of the City of Scotts Valley, it is not advisable to establish a spectrum of programs that target specific housing needs. Rather, it would be more cost efficient and more effective to establish the four delivery models described below and allow staff and the council to select the priorities annually. This model will allow non-profit and for-profit developers to apply for specific program funds, i.e. predevelopment, gap, site acquisition or silent seconds. The City would then be able to establish initially a standard set of loan documents and agreements that can be applied to the specific loan type. This will greatly reduce the legal costs attributable to such programs.

Gap Financing

| | |
|---------------------|--|
| Program Objective | Provide debt financing for the construction of rental housing with the prescribed affordability goals. |
| Program Description | The City will provide permanent financing in a junior position in new rental projects. |
| Terms | Deferred payment for five years, 3% simple interest loans. Repayment options that do not jeopardize affordability will be available thereafter. Minimum 20 years affordability. Level payments on principal and interest amortized over 30 years or more. Option to renew term on a project-by-project basis. |
| Eligible Borrower | Non-profit, for-profit developers and joint ventures. |

| | |
|----------------------|---|
| Eligible Properties | Multi-Family rental projects with 5+ units. Projects may contain commercial space but the costs attributable to the commercial portion cannot be financed with City funds. Mobile home parks acquired by non-profit owner organizations. |
| Security | The City will consider second, third or lower lien position on a project by project basis. |
| Loan To Value Ratio | The City will consider 100% loan to value only for non-profit developers. For-profit developers the City will not consider a loan to value ration on combined debt of lower than 90%. |
| Debt Coverage Ratio | The City does not have a debt to coverage ratio but will take it into account if a the developer is considering a conventional first mortgage with prescribed debt to coverage ratios. |
| Loan Fees | The City does not charge any loan fees. |
| Commitment Term | The developer will enter into an agreement to perform on a specific schedule. All commitments will have a maximum term of 24 months. |
| Appraisals | The City will use the appraisals available for the project. If no appraisal is available an appraisal will be required at the cost of the applicant. |
| Environmental Policy | Prior to firm commitment all borrowers will be required to provide the necessary toxic and environmental clearances. |
| Occupancy | Within Article XXXVI provisions, provide a minimum of 49% of the units: 29% at 80% of median or below, 20 at 50% of median or below. |
| Developer Fees | Developer fees in Low Income Housing Tax Credit projects will be limited to the California Tax Allocation Committee requirements of 15% of the eligible basis before the developer fee. All other projects will have a developer fee limited to \$500 per unit. |

Limited Partnerships

The City will carefully evaluate the inter and intra partnership distributions. Funds segregated for specific time periods and then released to one of the partners will have to be used to first pay any outstanding interest and or principle on the City loan and second used to develop projects in Scotts Valley. Under no circumstances will the City allow funds which were raised by a Scotts Valley project to be used in developing a project outside the City.

Predevelopment

Program Objective

To provide funds for predevelopment costs associated with projects by non-profit developers.

Program Description

The City will make secured predevelopment loans to qualified non-profit developers which may eventually become permanent Gap loans under the Gap loan Program

Terms

24 month terms at current rate on funds invested.

Eligible Participants Term

Non-profit developers with a proven track record in development. Deferred payment for 24 months. Upon City approval loans (see previous program description). If the loan is repaid at the end of the predevelopment term the interest rate will be 3% simple interest.

Level payments on principal and interest amortized over 5 years may be the other option.

Option to renew term on a project-by-project basis.

The deed and covenant restrictions will remain on the property even if the City funds are repaid.

Eligible Borrowers

Non-profit developers and joint ventures where the general partner is a non-profit developer.

| | |
|----------------------|--|
| Eligible Properties | Multi-Family rental projects with 5+ units. Projects may contain commercial space but the costs attributable to the commercial portion cannot be financed with City "affordable housing" funds. Mobile home parks acquired by non-profit owners. |
| Security | All predevelopment loans must be secured. The City will consider second, third or lower lien position on a project by project basis. The predevelopment loan may be secured by a property which is owned by the non-profit and had adequate value. |
| Loan To Value Ratio | The City will consider 100% loan to value only for non-profit developers. For-profit developers the City will not consider a loan to value ratio on combined debt of higher than 90%. |
| Debt Coverage Ratio | The City does not have a debt to coverage ratio but will take it into account if a the developer is considering a conventional first mortgage with prescribed debt to coverage ratios. |
| Loan Fees | The City does not charge any loan fees. |
| Commitment Term | The developer will enter into an agreement to perform on a specific schedule. All commitments will have a maximum term of 24 months. |
| Appraisals | The City will use the appraisals available for the project. If an appraisal is available an appraisal will be required at the cost of the applicant. |
| Environmental Policy | Prior to release of funds all borrowers will be required to provide the necessary toxic and environmental clearances. |
| Occupancy | Within Article XXXVI provisions, provide a minimum of 49% of the units: 29% at 80% of median or below, 20 at 50% of median or below, |

Developer Fees

Developer fees in Low Income Housing Tax Credit projects will be limited to the California Tax Allocation Committee requirements of 15% of the eligible basis before the developer fee. All other projects will have a developer fee limited to \$500 per unit.

Limited
Partnerships

The City will carefully evaluate the inter and intra partnership distributions. Funds that segregated for specific time periods and then released to one of the partners will have to be used to first pay any outstanding interest and or principle on the City loan and second used to develop projects in Scotts Valley.

Eligible Uses:

Loan proceeds may be used for all predevelopment costs: site control, consultant fees including architectural, engineering, environmental and financial, environmental surveys, loan fees, TCAC fees, etc..

Release of Funds

All funds will be held by the City and will be released upon submission of appropriate invoices and progress reports.

Loan Amounts

A maximum loan amount of \$75,000 is available.

Site and Property Acquisition

Program Objective

To acquire land and or existing properties for affordable housing.

Program Description

The City will make secured acquisition loans to qualified developers for the acquisition of land and or existing properties.

Terms

Deferred payment for five years, 3% simple interest loans. Repayment options that do not jeopardize affordability will be available thereafter.

Minimum 20 years affordability.

| | |
|-----------------------|--|
| | Level payments on principal and interest amortized over 30 years. |
| | Option to renew term on a project-by-project basis. |
| Eligible Participants | Non-profit and for-profit developers with a proven track record in development. |
| Eligible Borrowers | For-Profit developers, non-profit developers and joint ventures where the general partner is a non-profit. All developers must evidence a proven track record in development. |
| Eligible Properties | Multi-Family rental projects with 2+ units. Projects may contain commercial space but the costs attributable to the commercial portion cannot be financed with City funds. Land that is appropriate for a new rental development and will be developed within 24 months of acquisition. Land banking is not an appropriate use of the funds. |
| Security | All acquisition loans must be secured. The City will consider second, third or lower lien position on a project by project basis. |
| Loan To Value Ratio | The City will consider 100% loan to value only for non-profit developers. For-profit developers the City will not consider a loan to value ration on combined debt of lower than 80%. |
| Debt Coverage Ratio | The City does not have a debt to coverage ratio but will take it into account if a the developer is considering a conventional first mortgage with prescribed debt to coverage ratios. |
| Loan Fees | The City does not charge any loan fees. |
| Commitment Term | The developer will enter into an agreement to perform on a specific schedule. All commitments will have a maximum term of 24 months. Failure to start construction within 24 months will result in default of the loan. |

| | |
|----------------------|---|
| Appraisals | The City will use the appraisals available for the project. If an appraisal is available an appraisal will be required at the cost of the applicant. |
| Environmental Policy | Prior to release of funds all borrowers will be required to provide the necessary toxic and environmental clearances. |
| Occupancy | <p>Within Article XXXVI provisions, provide a minimum of 49% of the units at acquisition:</p> <p>29% at 80% of median or below, 20 at 50% of median or below.</p> <p>Existing projects which do not meet these requirements at loan commitments must meet the requirement at loan closing.</p> |
| Developer Fees | Developer fees in Low Income Housing Tax Credit projects will be limited to the California Tax Allocation Committee requirements of 15% of the eligible basis before the developer fee. |
| Limited Partnerships | The City will carefully evaluate the inter and intra partnership distributions. Funds that are segregated for specific time periods and then released to one of the partners will have to be used to first pay any outstanding interest and or principle on the City loan and second used to develop projects in Scotts Valley. |
| Eligible Uses: | Loan proceeds may be used for all predevelopment costs: site control, consultant fees including architectural, engineering, environmental and financial, environmental surveys, loan fees, TCAC fees, etc.. |
| Release of Funds | All funds will be held by the City and will be released upon submission of appropriate invoices and progress reports. |

HOMEOWNERSHIP PROGRAM

The Second Mortgage Program

Deferred Second Mortgage (DSM): A deferred-payment second mortgage provided by the City will bridge the gap between the first mortgage a buyer can qualify for and the amount he/she needs to put down in order to afford the mortgage payments. In order to further lower costs for homebuyers, the City will also participate in the County's MCC program.

Eligible Buyers

1. First-time homebuyer: The buyer may not have had an ownership interest in a home during the past three years. The only exemption is for a displaced homemaker who is qualified to buy a home. A displaced homemaker is defined as an adult head of household who has not worked in the labor force for a number of years but has, during such years, worked primarily without remuneration to care for the home and family.
2. Moderate income buyers: The Homeownership program will have three eligible income categories between 120% and below. Income eligible for participation in this program will be adjusted periodically to agree with changes in the income requirements as they are adjusted by HUD.
3. Residence: The program is limited to persons/households who have lived or worked in County for a minimum of six months prior to applying for a DSM. Evidence of residence will be required.

Eligible Properties

1. Eligible properties: Owner-occupied single-family properties including single family detached homes, townhouses, and units in condominium developments. Multiple units and mobile home properties which are less than 400 square feet, 102 inches wide and are not of the type that is designed to be in a fixed location are ineligible for mortgage revenue bond financing and mortgage credit certificates, but may be eligible for redevelopment set aside funds.
2. Maximum Sales Price: The maximum sales price is based on the amount a household can afford to borrow, their downpayment and the City's second mortgage. If a household chooses to combine an MCC with the DSM then the purchase price cannot exceed the MCC purchase price or the price of the category.

The First Mortgages

1. Participants may qualify for conventional fixed rate home mortgage loans, FHA or VA insured first mortgages. Borrowers and properties must meet standard underwriting criteria for conventional or government insured first mortgages.
2. Program applicants apply through participating program lenders for a first mortgage and the Second Mortgage Program .
3. MCC program participants must apply for a commitment through a lender participating in the Second Mortgage and the MCC program.
4. Loan Amount: Borrowers who qualify within established income parameters will be eligible for up to a \$20,000 second mortgage.
5. Loan Terms: The loans have deferred interest and principal for five years. The interest rate is 5% simple interest. At the beginning of year six, borrowers may pay off the City's loan in monthly payments fully amortized over fifteen-year period or choose to defer payment until sale, transfer, change of occupancy or the end of the loan term, in year 20.

If the borrower chooses to defer the payments to year twenty then the City will charge 5% interest or a proportionate share of the appreciation whichever is greater. The interest rate for Borrowers who elect to amortize the loan at year six for the first five years will be forgiven.

The maximum City loan term will be 20 years. Within 20 years, all outstanding principal and interest on the City loan will be due and payable. The City will assess the borrower's ability to start the monthly payments based on income at year five. Special hardship provisions will be available to assist households in financial difficulty or those who cannot bear additional housing costs.

Example A: Borrower chooses to amortize the loan at year six.

Original loan amount: \$20,000
Fifteen year amortization payments: \$158
Total paid back to the City: \$28,440

Example B: Borrower chooses to defer loan. On year 20 or upon sale or transfer, the borrower will have to pay the following:

Original loan amount: \$20,000
Loan fixed rate: 5%
Repayment of interest and principal: \$40,000
Appreciation: Original Purchase price \$100,000
Sales Price at year 20: \$200,000
Proportionate share of City's loan: 50 %
Appreciation: \$100,000
Proportionate share of City's
appreciation: \$50,000
Repayment of City second interest and
principal: \$90,000
Borrower's pays higher of the two: \$90,000

6. Loan Costs: All loan closing, escrow and loan document costs for the second mortgage will be paid by the borrower out of the second mortgage proceeds.
7. Lender/Servicer: The City has contracted with two lenders to originate and one servicer for the second mortgages.
8. Loan to Value: The program allows for up to a 95% combined loan to value ratio with a minimum 5% down-payment by the borrower.

MARKETING AND SELECTION

Marketing

The Program will be marketed through local realtors, employers, newspapers, community organizations and public service announcements. A program information brochure will be available to applicants with the hotline number available for questions.

1. The Program will be announced at a press conference with program start date to follow.
2. This method will give all potential applicants an equal chance at being "qualified applicants".

The Process

1. Interested persons will call the program hotline number for general information and a program application packet which will include the brochure with the program application.
2. Potential applicants must attend one of the two home ownership seminars to be sponsored by the City and the participating lenders.
3. The seminars and the hotline will be available to answer questions and determine preliminary eligibility.
4. Applicants must be prequalified by a lender and sign an application affidavit before a specific date.
5. The borrowers will submit the application to the City with all the verifications for income and ownership for a DSM commitment.
6. City staff will review the application and issue a 60-day DSM reservation by category. If a category has a large number of applicants staff will draw names from the list of qualified applicants.
7. The applicant must close the transaction within 60 days of the City's commitment. If an applicant fails to complete the transaction, the City will recapture the funds reserved.

Program Administration

Typically second mortgage programs require that one staff person is involved in the design and administration of the program in order to assure a smooth and successful implementation. A program this size will initially need one employee on an hourly contract with the potential to provide additional hours during the first two months of the program at a fixed 20 hours per week for a total of six months. The staff will need to be involved in the following:

- Preparation of loan documents.
- Negotiations with lenders.
- Lender staff training.
- Preparation of application packages and marketing materials, which includes pricing and production of brochures and forms.
- Marketing of the program to realtors and homeowners.
- Conducting homeownership seminars to potential applicants.
- Answering daily questions from applicants, lenders and realtors.
- Issuing commitments to qualified borrowers.
- Reviewing applications and hearing appeals from applicants.
- Implementing a system for fund withdrawals from the City to the lenders.
- Establishing the ongoing monitoring system for the loans closed.
- Making and establishing policy calls from lenders and borrowers. Establishing program policies in an ongoing record.

Additionally, legal counsel must draft the following documents: Promissory Note and Deed of Trust and Loan origination and servicing agreements.

APPENDIX "A"

Assume the construction of a 15 unit apartment development consisting of 15 two bedroom units. Twenty percent (3 units) of all units will be rented to very low-income households at affordable rents; the balance will be available at market rents.

Monthly rents are as follows:

| <u>Two Bedroom</u> | |
|--------------------|---------------|
| <u>Affordable</u> | <u>Market</u> |
| \$499 | \$900 |

These rents result in a total monthly gross income of \$12,297. Subtracting out amounts for vacancy (5%), operating expenses (30%), and debt service coverage (1:1.10) results in \$7,288 being available monthly to service debt. The mortgage supportable by this amount assuming a 30 year amortization schedule (although the loan would normally have a call date at the end of 15 years and an interest rate of 8.5%) is \$947,830. If we assume a per unit development cost of \$85,017, for a total project cost of \$1,275,257, we have a shortfall of \$327,427.

Of course, few, if any, developers can obtain 100% financing for their project and usually contribute some equity themselves. Assuming their equity contribution is equal to 15% of the total development cost (\$191,000) still leaves a gap of \$136,427. If that same developer was to develop the project as a 100% market rate project his gap would be zero.

The following analysis shows the referenced project at 100% Market Rate compared to 20% Affordable @ 50% of Median. In this situation there is not a "feasibility gap" but there is an "affordability gap":

Appendix "A" cont.

Affordable Arms
Scotts Valley, California

| | 20% Affordable @ 50% of Median | 100% Market Rate Project |
|--|--------------------------------------|-----------------------------|
| Monthly Gross Income | | |
| Affordable Units | 1,497 | 0 |
| Market | <u>10,800</u> | <u>13,500</u> |
| Total Income | 12,297 | 13,500 |
| Less 5% Vacancy Allowance | <u><615></u> | <u><675></u> |
| Effective Gross Income | 11,682 | 12,825 |
| Less Operating Expenses | <u><3,562></u> | <u><3,562></u> |
| Net Operating Income | 8,120 | 9,263 |
| Less Debt Service Coverage | <u><832></u> | <u><926></u> |
| Available for Debt Service | 7,288 | 8,337 |
| Supportable Mortgage at 8.5% (over 30 years) | 947,830 | 1,084,257 |
| Developer's Equity @ Approx. 15% | <u>191,000</u> | <u>191,000</u> |
| Total Sources | 1,138,830 | 1,275,257 |
| Total Development Cost | 1,275,257 | 1,275,257 |
| Less Total Sources | <1,138,830> | <1,275,257> |
| Shortfall due to Affordability | 136,427 | 0 |
| Shortfall due to Feasibility | 0 | 0 |

If this project had a feasibility gap, typically the City would choose not to cover that gap; rather, the City would only cover the gap created by the affordability requirements.

The City funds may be leveraged with other federal, state and or conventional lender products. In the current universe of affordable housing development all projects combine a variety and type of resources.